United Nations E/C.18/2007/10

Economic and Social Council

Distr.: General
21 August 2007

Original: English

Committee of Experts on International Cooperation in Tax Matters
Third session
Geneva, 29 October-2 November 2007

Proposed commentary on article 26 (proposed 2007) of the United Nations Model Double Taxation Convention between Developed and Developing Countries

Proposed general considerations and commentary on paragraphs 1-3 prepared by the Interim Coordinator of the Subcommittee on Exchange of Information*

Summary

The proposed general considerations and commentary on article 26 (proposed 2007) of the United Nations Model Double Taxation Convention between Developed and Developing Countries, paragraphs 1 to 3, are set out below. The proposed commentary discusses the intended purpose of article 26, its scope, the confidentiality requirements for information obtained under article 26, and the exceptions that a Contracting State may invoke to avoid complying with a request for information.

The proposed commentary on article 26 (proposed 2007), paragraphs 4 to 7, and the inventory of exchange mechanisms, is contained in document E/C.18/2007/11.

* The present note has not yet been acted upon by the full Subcommittee. All comments received from members of the Subcommittee are reflected in the document. The views and opinions expressed are those of the authors and do not necessarily represent those of the United Nations.

07-48750 (E) 190907

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* See E/C.18/2007/11.

Proposed United Nations commentary

Article 26
Exchange of information[1]

General considerations

1. Article 26 embodies rules under which information may be exchanged to the widest possible extent, both to facilitate the proper application of the treaty and to assist the Contracting States in the enforcement of their domestic tax laws. Consequently, the obligation to exchange information under this article should be interpreted broadly, and the limitations on that obligation should not be extended by analogy beyond their specific meaning. In particular, the article should be understood to require the Contracting States to promote an effective exchange of information.

1.1. In a global economy, cooperation among nations on fiscal matters has become increasingly important, and the former reluctance of nations to concern themselves with the revenue laws of other countries mostly has disappeared. Article 26 provides a basis for the effective exchange of information between the Contracting States, whereas article 27 provides for assistance in collection. From the perspective of many developing countries, article 26 is particularly important not only for curtailing cross-border tax evasion and avoidance but also to curtail the capital flight that is often accomplished through such evasion and avoidance.

1.2. Much of the language of article 26 is also found in the comparable article of the OECD Model Convention. Consequently, the OECD commentary to that article generally is relevant in interpreting article 26 of the United Nations Model Convention. It should be understood, nevertheless, that article 26 is intended to be broader in a number of respects than the comparable provision in the OECD Model Convention.

1.3. Although article 26 imposes reciprocal obligations on the Contracting States, it does not allow a developed country to refuse to provide information to a developing country on the ground that the developing country does not have an administrative capacity comparable to the developed country. Reciprocity has to be measured by reference to the overall effects of a treaty, not with respect to the effects of a single article.

1.4. The text of paragraph 1 of article 26 makes clear that the exchange of information is not restricted by article 1 (Persons covered) or article 2 (Taxes covered). Consequently, the information exchanged may relate to persons who are not resident in either Contracting State and to the administration or enforcement of taxes not mentioned in article 2. Some countries may object to the extension of paragraph 1 to all taxes, for constitutional reasons or other reasons. Those concerns are addressed in section B below.

1.5. Following the pattern of the 2005 OECD revisions, paragraph 1 of article 26 was broken up into three separate paragraphs, now paragraphs 1, 2 and 7. That paragraphing change was made for clarity and has no substantive significance.

[1] Coordinator's draft of 16 August 2007.

2. Article 26 was modified substantially in 2007 with a view to clarifying certain issues, expanding the scope of the article and limiting exceptions to the obligation to exchange information. In some cases, the changes made were not intended to be substantive but rather were intended to remove doubts as to the proper interpretation of the article. For example, the term "necessary" in paragraph 1 was changed to "may be relevant" to clarify the intended meaning of the prior language. In contrast, the change in that paragraph providing for an exchange of information with respect to taxes not mentioned in article 2 was intended to be a substantive change.

2.1. In some cases, the issue of whether a change made to article 26 is intended as substantive or interpretative depends on the prior practices of the Contracting States. For example, in some cases, the addition of paragraph 5, which removes, inter alia, domestic bank secrecy laws as a basis for refusing to exchange information, may simply clarify the meaning of the limitations on the exchange of information contained in paragraph 3. In other cases, it may modify that paragraph substantively. The effect of the change depends in part on the particular prior practices of the Contracting States. The position taken in the OECD commentary is that paragraph 5 is primarily interpretative with respect to treaties between its member States. This issue may be of particular importance in interpreting treaties that were entered into prior to the adoption of the 2007 changes to article 26.

2.2. One difference in the wording of article 26 and the comparable provision of the OECD Model Convention is that article 26 includes in paragraph 1 the following sentence: "In particular, information shall be exchanged that would be helpful to a Contracting State in preventing fraud or evasion of such taxes or in combating tax avoidance." The phrase "or combating tax avoidance" was inserted in 2007. That change was thought to be useful by members of the Committee, especially members from developing countries, to make clear in the text of article 26 a point that was already clear in the United Nations commentary and was implicit in the language of the last sentence of prior paragraph 1, now moved to paragraph 7. The statement of the purposes of information exchanges in the text of article 26 is intended to provide guidance to the Contracting States on the proper interpretation of the article.

2.3. Although tax evasion is illegal and tax avoidance is not, both result in the same loss of revenue to the Government and, by definition, both defeat the intent of the Government in enacting its taxing statutes. Consequently, mutual assistance in combating tax avoidance is an important aspect of mutual cooperation on tax matters. In addition, some forms of aggressive tax avoidance are so close to the line between avoidance and evasion that a Contracting State is unlikely to know for sure whether the information it is requesting deals with avoidance or evasion until after it obtains the requested information. Information on tax avoidance may be extremely useful to a Contracting State in its efforts to close possible loopholes in its taxing statutes.

3. The term "exchange of information" should be understood broadly to include an exchange of documents and an exchange of information unrelated to specific taxpayers.

3.1. If specifically requested by the competent authority of a Contracting State, the competent authority of the other Contracting State should provide information under article 26 in the form of depositions of witnesses and authenticated copies of unedited original documents (including books, papers, statements, records, accounts or writings), to the extent feasible. Under paragraph 3, the requested State may

decline to provide the information in the specific form requested if, for instance, the requested form is not known or permitted under its law or administrative practice. A refusal to provide the information in the form requested does not affect the obligation to provide the information.

3.2. Contracting States may wish to use electronic or other communication and information technologies, including appropriate security systems, to improve the timeliness and quality of exchanges of information. Indeed, the Contracting States may be obligated to provide requested information in electronic form if such action is necessary for an effective exchange of information. Contracting States which are required, according to their law, to observe data protection laws, may wish to include provisions in their bilateral conventions concerning the protection of personal data exchanged. Data protection concerns the rights and fundamental freedoms of an individual, and in particular, the right to privacy, with regard to automatic processing of personal data. In no event is a Contracting Party relieved of its obligation to exchange information simply because its domestic laws do not allow it to provide the information in the form requested.

3.3. The scope of exchange of information covers all tax matters without prejudice to the general rules and legal provisions governing the rights of defendants and witnesses in judicial proceedings. Exchange of information for criminal tax matters can also be based on bilateral or multilateral treaties on mutual legal assistance (to the extent they also apply to tax crimes).

3.4. Article 26 specifically provides for the exchange of information in at least three modes: exchange by specific request, automatic exchange, and other exchanges, understood to include spontaneous exchanges. According to the commentary to the OECD Model Convention, that same result is reached by implication, without any specific language authorizing the three modes of exchange in the text of the OECD Model Convention. It is anticipated that the competent authorities will adopt procedures that will provide for the mode of exchange best suited to achieve an effective exchange of information.

3.5. Nothing in the United Nations Model Convention prevents the application of the provisions of article 26 to the exchange of information that existed prior to the entry into force of the Convention, as long as the assistance with respect to this information is provided after the Convention has entered into force and the provisions of the article have become effective. Contracting States may find it useful, however, to clarify the extent to which the provisions of the article are applicable to such information, in particular when the provisions of that Convention will have effect with respect to taxes arising or levied from a certain time.

4. The Committee has suggested some guidelines for arrangements regarding the implementation of appropriate exchanges of information (see sect. C below). Those guidelines are in the form of an inventory of options available to the competent authorities. The inventory is not intended to be exhaustive or to impose any procedural obligations on a Contracting State. Instead, the inventory is a listing of suggestions to be examined by competent authorities in developing procedures for an effective exchange of information.

Commentary on paragraphs 1-3 of article 26 (proposed 2007)

Paragraph 1
General rule

5. The first sentence of paragraph 1 sets forth the basic obligation of the Contracting States concerning the exchange of information. It requires, subject to the limitations of paragraph 3, that the competent authorities exchange such information as may be relevant for the proper application of the Convention or for the administration or enforcement of their domestic tax laws, as long as taxation under those laws is not inconsistent with the Convention.

5.1. Prior to the 2007 changes to article 26, the term "necessary" was used instead of the term "may be relevant". The view of the Committee and the OECD commentary has been that these terms have similar if not identical meanings. That is, the term "necessary" is understood to mean "appropriate and helpful", not "essential". In any event, whatever the phrase chosen, the requesting State is not obliged to demonstrate its need for the requested information before the obligation to provide that information arises.

5.2. The standard of "may be relevant" is intended to provide for exchange of information in tax matters to the widest possible extent and, at the same time, to clarify that Contracting States are not at liberty to request information about a particular taxpayer that is highly unlikely to be relevant to the tax affairs of that taxpayer. Contracting States may agree to an alternative formulation of this standard that is consistent with the scope of the article. For example, they might replace "may be relevant" with "necessary" or "relevant" or "foreseeably relevant" (the OECD formulation) if those terms are understood to require an effective exchange of information. In the interests of clarity, however, the term "may be relevant" is preferred.

5.3. The information covered by paragraph 1 is not limited to taxpayer-specific information. The competent authorities may also exchange other sensitive information related to tax administration and compliance improvement, for example, risk analysis techniques or tax avoidance or evasion schemes. They may also share information they have obtained about aggressive tax avoidance schemes, such as those promoted by some international accounting firms. In addition, the competent authorities may exchange information relating to a whole economic sector (e.g., the oil, fishing or pharmaceutical industry, the banking sector etc.) and not to particular taxpayers.

6. The scope of the obligation to exchange information is not limited by articles 1 or 2. That is, the obligation applies not only with respect to information relevant to the proper application of the Convention or to the administration or enforcement of domestic taxes mentioned in article 2 but also to all other domestic taxes, including subnational taxes. In this respect, the United Nations Model Convention and the OECD Model Convention, as amended in 2005, are identical.

6.1. Some members of the committee from developing countries expressed concern that sharing of information with respect to all taxes, particularly subnational taxes, might prove burdensome or might raise constitutional and political issues for them. They suggested that the obligation to provide information might be limited to taxes covered by the Convention plus one or two important taxes, such as the value-added

tax (VAT). To accomplish that outcome, the following language might be substituted for paragraph 1:

> "1. The competent authorities of the Contracting States shall exchange such information as may be relevant for carrying out the provisions of this Convention or for the administration or enforcement of the domestic laws of the Contracting States *concerning taxes covered by the Convention and [insert specific taxes] of a Contracting State*, in so far as the taxation thereunder is not contrary to the Convention."

6.2. The obligation to provide requested information applies whether or not the person, with respect to whom the information is requested, is a resident of either Contracting State or is engaged in economic activity in either Contracting State. For example, a Contracting State may request information about the bank deposits of an individual who is resident in some third State.

7. The obligation imposed under paragraph 1 is for an *effective* exchange of information. A Contracting State may not avoid its obligations under paragraph 1 through unreasonable time delays or by imposing unreasonable or burdensome procedural barriers.

8. The examples provided in paragraphs 8.1 and 8.2 below illustrate the application of paragraph 1 of the Convention in particular cases. Some of these examples are drawn from, but are not identical to, the examples provided in paragraphs 6 and 7 of the OECD commentary on article 26. In all of these examples, the requested State (the Contracting State that has been asked for information) has the obligation under paragraph 1 of the Convention to provide the requested information.

8.1. Application of the Convention (between State A and State B):

(a) State A, where the recipient of royalties under a royalty contract is resident, is attempting to apply article 12 (Royalties). It asks State B, where the payer of the royalty is resident, for information concerning the amount of royalty transmitted.

(b) In deciding whether it is proper to grant to the recipient of a royalty the relief claimed under article 12, State B asks State A whether the recipient is in fact a resident of State A and is the beneficial owner of the royalties.

(c) In computing the taxable profits of a permanent establishment that is located in State A and has its head office in State B, State A may request information from State B about the expenses and profits of the head office and the dealings of the head office with other permanent establishments and associated companies.

(d) Similarly, if an associated company, within the meaning of article 9, is located in State A and another associated company is located in State B, then State A may request information from State B about the profits and expenses of the associated company located in State B and about the dealings of that associated company with any other associated companies and permanent establishments.

(e) State A or State B may request information that may be relevant for the purposes of applying article 25 (Mutual agreement procedure).

(f) State B is attempting to tax an employee resident in State A in accordance with article 15 (Dependent personal services). The employment has been

exercised for more than 183 days in State B. That State may request that State A provide it with information on the amount of the income exempted from taxation in State A in accordance with article 23 A (Exemption method for relieving double taxation).

(g) State A is attempting to impose a corporate income tax on an entity claiming to be a partnership. State A may request information from State B that would be helpful to it in properly classifying the entity for tax purposes, including information about the way the entity is classified for tax purposes by State B.

(h) State A is being asked to provide to one of its residents a tax credit under article 23 B for income taxes allegedly paid to State B. State A may request from State B information about whether the alleged payment of the tax actually occurred.

8.2. Implementation of domestic laws:

(a) A company in State A supplies goods to an independent company in State B. State A wishes to know from State B what price the company in State B paid for the goods supplied, with a view to a correct application of the provisions of its domestic value-added tax.

(b) A company in State A sells goods through a company in State C (possibly a low-tax country) to a company in State B. The companies may or may not be associated. There is no convention between State A and State C, nor between State B and State C. Under the Convention between State A and State B, State A, with a view to ensuring the correct application of the provisions of its domestic laws to the profits made by the company situated in its territory, asks State B what price the company in State B paid for the goods.

(c) State A, for the purpose of taxing a company situated in its territory, asks State B, under the convention between A and B, for information about the prices charged by a company in State B, or a group of companies in State B with which the company in State A has no business contacts in order to enable State A to check the prices charged by the company in that State by direct comparison (e.g., prices charged by a company or a group of companies in a dominant position).

(d) A resident of State A holds a bank account in State B and the income from that account is exempt from tax under the domestic laws of State B. State A may request that State B provide information on the amount of interest income earned on that account.

(e) A financial intermediary invests money of its account holders in State A, earning therein dividends and interest. State A requires that the financial intermediary keep records of the beneficial owners of the accounts but does not routinely request those records in enforcing its domestic laws. State B suspects that some of the beneficiaries of the account holders of the financial intermediary are its residents and are properly taxable under its domestic laws. State B may request that State A obtain for it the information about the account holders from the financial intermediary.

(f) A corporation resident in State A has affiliated companies located in State B and State C. State B believes that the affiliated company doing business in its territory has been skimming profits into the affiliated company located in State C. State B may request that State A provide it with information about the profits and expenses of the affiliated company located in State C.

Paragraph 2
Obligation to confidentiality

9. A Contracting State cannot be expected to provide confidential financial information to another Contracting State unless it has confidence that the information will not be disclosed to unauthorized persons. To provide the assurance of secrecy required for effective information exchange, paragraph 2 provides that information communicated under the provisions of the convention shall be treated as secret in the receiving State in the same manner as information obtained under the domestic laws of that State. Sanctions for the violation of such secrecy in that State will be governed by the administrative and penal laws of that State.

10. Of course, the information received under article 26 would be useless to the requesting State (the Contracting State requesting the information) if the prohibition against disclosure were absolute. Paragraph 2 provides that information received under article 26 can be disclosed to persons and authorities involved in the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes mentioned in paragraph 1. In addition, it is understood that the information may also be communicated to the taxpayer, his proxy, or to witnesses in a civil or criminal proceeding.

10.1. As stated in paragraph 10, the information obtained can be communicated to the persons and authorities mentioned and on the basis of the last sentence of paragraph 2 of the article can be disclosed by them in court sessions held in public or in decisions which reveal the name of the taxpayer. Once information is used in public court proceedings or in court decisions and thus rendered public, it is clear that from that moment such information can be quoted from the court files or decisions for other purposes even as possible evidence. But this disclosure to the public does not mean that the persons and authorities mentioned in paragraph 2 are allowed to provide on request additional information received.

10.2. If either or both of the Contracting States object to information obtained under article 26 being made public by courts, or, once the information has been made public in this way, to the information being used for other purposes, they should state this objection expressly in their convention.

11. In general, the information received by a Contracting State may be used only for the purposes mentioned in paragraph 1. If the information appears to be of value to the receiving State for purposes other than those referred to in that paragraph, that State may not use the information for such other purposes without the authorization of the competent authority of the supplying State. That authorization should not be unreasonably withheld.

11.1. In some cases, a Contracting State may prosecute a taxpayer for tax evasion and also for an additional crime, such as money-laundering, that arises out of the same set of facts. In such circumstances, the receiving State may use the information provided for both purposes.

11.2. The information received by a Contracting State may not be disclosed to a third country without the authorization of the competent authority of the other Contracting State unless there is an express provision in the bilateral treaty between the Contracting States allowing such disclosure.

11.3. Contracting States wishing to broaden the purposes for which they may use information exchanged under this article may do so by adding the following text to the end of paragraph 2:

> "Notwithstanding the foregoing, information received by a Contracting State may be used for other purposes when such information may be used for such other purposes under the laws of both States and the competent authority of the supplying State authorises such use."

12. The OECD Model Convention, as amended in 2005, includes a provision that would allow the sharing of information obtained under article 26 with persons charged with the oversight of the persons allowed to obtain such information. That provision is not included in paragraph 2, due to opposition from some members of the Committee from developing countries, who feared that the oversight bodies, which typically are political entities, would not be subject under domestic law to the same strict rules of confidentiality as tax officials.

12.1. Excluding oversight bodies from the persons entitled to receive confidential information obtained through information exchange presents problems in some countries because their oversight bodies typically expect to have access to such information in order to fulfil their oversight duties. Contracting States wishing to address this issue without providing a blanket authorization for oversight bodies to receive confidential information might add the following language to the end of paragraph 2 of article 26:

> "In appropriate cases, the competent authorities may agree to allow the sharing of information received under paragraph 1 with an oversight body if that information is necessary for the oversight body to fulfil its oversight duties. In such cases, members of the oversight body must be subject to confidentiality requirements at least as strict as those applicable to tax administration and enforcement officials."

12.2. Countries wishing to adopt the position taken in the OECD Model Convention with respect to the sharing of information obtained under paragraph 1 with oversight bodies may modify paragraph 2 as follows (the changed language shown in italics):

> "2. Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State. However, if the information is originally regarded as secret in the transmitting State, it shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes referred to in paragraph 1, *or the oversight of the above*. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions."

12.3. If paragraph 2 is amended to authorize information to be disclosed to oversight bodies, that disclosure should be limited to information necessary for those bodies to fulfil their oversight duties. Such oversight bodies include authorities that supervise tax administration and enforcement authorities as part of the general administration of the Government of a Contracting State. Such sharing is permitted only if the persons engaged in oversight activities are subject to confidential requirements at least as strict as those applicable to tax administration and

enforcement officials. The competent authorities shall agree as to the bodies that constitute an oversight body within the meaning of this paragraph.

Paragraph 3
Limitations on obligation to exchange information

13. Paragraph 3 of article 26 contains provisions that limit the obligation of the requested State under paragraph 1. The limitations provided in paragraph 3, however, may be superseded by the provisions contained in paragraphs 4, 5 and 6. The provisions of paragraph 3, read in conjunction with the provisions of paragraphs 4, 5, and 6, should not be read in a way that would prevent an effective exchange of information between the Contracting States. In addition, a Contracting State must disclose to the other Contracting State before it enters into a convention any specific provisions of its laws and administrative practice that it believes entitle it to avoid an obligation otherwise imposed by paragraph 1.

14. Paragraph 3 (a), subject to the limitations provided in paragraphs 4, 5 and 6, contains the clarification that a Contracting State is not bound to go beyond its own internal laws and administrative practice in putting information at the disposal of the other Contracting State. For example, if a requested State is not permitted under its laws or administrative practice to seize private papers from a taxpayer without court authorization, it is not required to make such a seizure without court authorization on behalf of a requesting State even if the requesting State could make such a seizure without court authorization under its own laws or administrative practice. The purpose of this rule is to prevent article 26 from creating an unintentional conflict between a Contracting State's obligation under article 26 and its obligations under domestic law.

14.1. Domestic provisions requiring that information obtained by the tax authorities be kept secret should not be interpreted as constituting an obstacle to the exchange of information under paragraph 3 (a) because the tax authorities of the requesting State are obligated under paragraph 2 to observe secrecy with regard to information received under this article.

14.2. Paragraph 1 obligates a requested State to provide information with respect to all of the taxes of the requesting State even if the requested State does not have a comparable tax. Paragraph 3 (a) does not remove the obligation to provide information relating to taxes that the requested State does not impose. For instance, a requested State cannot avoid its obligation to provide information helpful to the requesting State in the enforcement of its value-added tax merely because the requested State does not have a value-added tax. Of course, the requested State may avoid the obligation to supply such information if it cannot obtain that information under its normal administrative procedures, within the meaning of paragraph 3 (b).

14.3. The purpose of paragraph 3 (a) is to avoid traps for the unwary, not to create such traps. A Contracting State that believes that it is not required to obtain certain types of information on behalf of the other Contracting State because of its own laws or administrative practice (including the laws and administrative practice of its subnational governments) must disclose that position in writing prior to entering into a convention containing article 26. It must also disclose the likely effects of that position on its ability to provide an effective exchange of information. For instance, if a Contracting State believes that one of its laws prevents it from providing the other Contracting State with information as to the beneficial owners of its resident

companies or other juridical persons, it is obligated to give written notice of that position during the negotiation of the convention, with an explanation of the impact of that law on its obligations in relation to mutual assistance. Depending on the facts and circumstances of the particular case, a failure to disclose may eliminate the right of a Contracting State to invoke paragraph 3 (a) to avoid its obligations under paragraph 1.

14.4. A Contracting State that changes its laws or administrative practice after entering into a convention containing paragraph 3 (a) must disclose that change to the other Contracting State in timely fashion. Depending on the facts and circumstances of the case, such a change may constitute a material breach of the convention. In any event, a failure to provide timely notice of such a change may eliminate the right of a Contracting State to invoke paragraph 3 (a) to avoid its obligations arising under paragraph 1.

14.5. A Contracting State that wishes to expand the scope of the limitation currently provided in paragraph 3 (a) might modify that subparagraph as follows (new language in italics):

> "(a) To carry out administrative measures at variance with the laws and administrative practice of that *Contracting State* or of the other Contracting State *even if that Contracting State knows and fails to disclose that specific provisions of its laws or administrative practice are likely to prevent an effective exchange of information*;"

15. Some countries are required by law to notify the person supplying information and/or the taxpayer subject to an enquiry prior to the release of that information to another country. Such notification procedures may be an important aspect of the rights provided under domestic law. In some cases, notification may help prevent mistakes (e.g., in cases of mistaken identity) and may facilitate exchange (by allowing taxpayers who are notified to cooperate voluntarily with the tax authorities in the requesting State). Notification procedures may not be applied, however, in a manner that, in the particular circumstances of the request, would frustrate the efforts of the requesting State to prevent fraud or evasion of taxes or to combat tax avoidance. That is, they should not prevent or unduly delay an effective exchange of information. For instance, notification procedures should permit exceptions from prior notification in cases in which the information request is of a very urgent nature or the notification is likely to undermine the chance of success of the investigation conducted by the requesting State.

15.1. A Contracting State that under its domestic law is required to notify the person who provided the information and/or the taxpayer that an exchange of information is proposed should inform its treaty partners in writing that it has this requirement and what the consequences are for its obligations in relation to mutual assistance. Such information should be provided to the other Contracting State before a convention is concluded and thereafter whenever the relevant rules are modified. Depending on the facts and circumstances of the particular case, a failure to disclose may eliminate the right of a Contracting State to invoke paragraph 3 (a) to avoid its obligations under paragraph 1.

16. In general, the requested State is not obligated to carry out administrative measures on behalf of the requesting State that are not permitted under the laws or administrative practice of the requesting State. Thus, a requested State that is

permitted under its own administrative practices to seize documents in the possession of a taxpayer without court authorization may refuse to seize such documents on behalf of a requesting State if the requesting State would be precluded by law from making such a seizure itself without court authorization. The purpose of this rule is to prevent a requesting State from using the administrative measures of the requested State to avoid limitations imposed on the requesting State by its own Government.

16.1. Different countries will necessarily have different mechanisms for obtaining and providing information. Variations in laws and administrative practice may not be used as a basis for the requested State to deny a request for information unless the effect of these variations would be to limit in a significant way the requesting State's legal authority to obtain and provide the information if the requesting State itself received a legitimate request from the requested State.

16.2. The general rule of paragraph 16 has no application when the legal system or administrative practice of only one country provides for a specific procedure. For instance, a Contracting State requested to provide information about an administrative ruling or advance pricing agreement (APA) it has granted cannot point to the absence of a ruling or APA regime in the requesting State to avoid its obligation under paragraph 1 to provide such information.

17. Most countries recognize under their domestic laws that information cannot be obtained from a person to the extent that such person can claim the privilege against self-incrimination. A requested State, therefore, may decline to provide information if its self-incrimination rules preclude it from obtaining that information or if the self-incrimination rules of the requesting State would preclude it from obtaining such information under similar circumstances. In practice, however, the privilege against self-incrimination should have little, if any, application in connection with most information requests. The privilege against self-incrimination is personal and cannot be claimed by an individual who himself is not at risk of criminal prosecution. In the overwhelming majority of information requests, the objective is to obtain information from third parties such as banks, intermediaries, or the other party to a contract and not from the individual under investigation. Furthermore, the privilege against self-incrimination generally does not attach to persons other than natural persons.

18. Subparagraph 3 (b) allows a requested State to avoid an obligation otherwise imposed by paragraph 1 when it cannot obtain the requested items of information in the normal course of its administration or when the other Contracting State could not have obtained that information in the normal course of its administration. The purpose of this rule is to prevent the requesting State from imposing unreasonable burdens on the requested State.

18.1. Information is deemed to be obtainable in the normal course of administration if the information is in the possession of the tax authorities or can be obtained by them in the normal procedure of tax determination, which may include special investigations or special examination of the business accounts kept by the taxpayer or other persons. For instance, if the requested State, as part of its audit policies, obtains information about the appropriateness of the transfer prices used by its taxpayers in dealings with associated companies, it is deemed to be able to obtain similar information about its taxpayers and associated companies on behalf of a requesting State.

18.2. Unless otherwise agreed to by the Contracting States, it can be assumed that the information requested by a Contracting State could be obtained by that State in a similar situation unless that State has informed the other Contracting State to the contrary.

18.3. It is often anticipated, when a Convention is entered into between a developed country and a developing country, that the developed country will have a greater administrative capacity than the developing country. Such a difference in administrative capacity does not provide a basis under subparagraph 3 (b) for either Contracting State to avoid an obligation to supply information under paragraph 1. That is, paragraph 3 does not require that each of the Contracting States receive reciprocal benefits under article 26. In freely adopting a Convention, the Contracting States presumably have concluded that the Convention, viewed as a whole, provides each of them with reciprocal benefits. There is no presumption, however, that each of the articles, or each subparagraph of each article, provides a reciprocal benefit. On the contrary, it is commonplace for a Contracting State to give up some benefit in one article in order to obtain a benefit in another article. Reading a specific reciprocity requirement into paragraph 3 of article 26 would be inconsistent with the normal understanding of how convention negotiations are conducted.

18.4. Although subparagraphs 3 (a) and 3 (b) do not explicitly provide for reciprocity in benefits, the OECD commentary to article 26 has taken the position that a reciprocity requirement can be inferred from the language of subparagraph 3 (b), which, inter alia, limits the obligation of a Contracting State to supply information obtainable in the normal course of administration of that other Contracting State. In effect, the OECD commentary is reading the term "obtainable" to mean that the other Contracting State has the actual administrative capacity to obtain that information. The alternative reading is that "obtainable" means that the tax administration has the authority to obtain the information, whether or not it has the capacity to exercise that authority. As noted above, this latter reading is more consistent with the purpose of article 26. It should also be noted that the OECD commentary has interpreted the alleged reciprocity requirement narrowly to prevent it from reducing article 26 to a nullity.

18.5. In the light of the position taken in the OECD commentary, some countries may wish to clarify the matter of a reciprocity requirement by amending subparagraph 3 (b) to read as follows:

> "(b) To supply information that cannot be obtained in the normal course of the administration of that Contracting State or is not obtainable under the laws of that Contracting State or of the other Contracting State;"

19. In general, a requested State may decline, under paragraph 3 (b), to disclose information that constitutes a confidential communication between an attorney, solicitor or other admitted legal representative in his role as such and his client to the extent that the communication is protected from disclosure under domestic law.

19.1. The scope of protected confidential communications should be narrowly defined. Such protection does not attach to documents or records delivered to an attorney, solicitor or other admitted legal representative in an attempt to protect such documents or records from disclosure required by law. Also, information on the identity of a person, such as a director or beneficial owner of a company, is not protected from disclosure. Although the scope of protection afforded under domestic

law to confidential communications may differ among States, the protection provided under subparagraph 3 (b) does not extend so broadly so as to hamper the effective exchange of information.

19.2. Notwithstanding the provisions of domestic law in the requested State, that State may decline to supply requested communications between attorneys, solicitors or other admitted legal representatives and their clients only if, and to the extent that, such representatives act in their capacity as attorneys, solicitors or other admitted legal representatives and not in a different capacity, such as nominee shareholders, trustees, settlors, company directors or accountants, or under a power of attorney to represent a company in its business affairs. More specifically, the communication must have been produced in good faith for the purpose of seeking or providing legal advice or for use in existing or contemplated legal proceedings.

19.3. In no event may a requested State decline to disclose communications between attorneys, solicitors or other admitted legal representatives and their clients if those persons have themselves participated with their clients in a plan to commit tax evasion or fraud.

19.4. A claim that information is protected as a confidential communication between an attorney, solicitor or other admitted legal representative and its client should be adjudicated exclusively in the Contracting State under the laws of which the claim arises. Thus, it is not intended that the courts of the requested State should adjudicate claims based on the laws of the requesting State.

20. Subparagraph 3 (c) permits a requested State to decline to provide information if the disclosure of that information would reveal any trade, business, industrial, commercial or professional secret or trade process. Before invoking this provision, a Contracting State should carefully weigh if the interests of the taxpayer really justify its application. Secrets mentioned in this subparagraph should not be taken in too wide a sense. A wide interpretation of the provision in many cases would be inconsistent with the purpose of article 26 because it would render ineffective the exchange of information provided for in that article.

20.1. A trade or business secret or trade process is generally understood to mean information which has considerable economic importance and which can be exploited practically and the unauthorized use of which may lead to serious damage (e.g., may lead to severe financial hardship). The purpose of the secrecy exception is to prevent an exchange of information from imposing unfair hardship on taxpayers by revealing to their competitors or potential competitors valuable secret information and thereby significantly diminishing the commercial value of that information. Secret information that once had substantial commercial value may be disclosed if that information does not have substantial commercial value at the time the information is requested. Information is not secret within the meaning of subparagraph 3 (c) simply because the disclosure of it would be embarrassing to the taxpayer or to a third party or may result in the taxpayer having to pay additional taxes. A Contracting State may decide to supply requested information when it finds that there is no reasonable basis for assuming that the taxpayer involved may suffer adverse consequences incompatible with information exchange.

20.2. Secret information may be disclosed to the requesting State if the requested State determines that the risk of disclosure to the public or to competitors is highly unlikely due to the confidentiality requirements set forth in paragraph 2. A

document that is protected from full disclosure because it contains protected secret information may be disclosed if the secret information is removed.

20.3. Financial information, including books and records, does not by its nature constitute a trade, business or other secret. In certain limited cases, however, the disclosure of financial information might reveal a trade, business or other secret. For instance, a request for information on certain purchase records may raise such an issue if the disclosure of such information would reveal the proprietary formula used in the manufacture of a product. The protection of such information may also extend to information in the possession of third persons. For instance, a bank might hold a pending patent application for safe keeping, or a secret trade process or formula might be described in a loan application or in a contract held by a bank. In such circumstances, details of the trade, business or other secret should be excised from the documents and the remaining financial information exchanged accordingly.

21. Paragraph 3 (c) also includes a limitation with regard to information which concerns the vital interests of the State itself. Under that limitation, Contracting States do not have to supply information the disclosure of which would be contrary to public policy (*ordre public*). This limitation should only become relevant in extreme cases. For instance, such a case could arise if a tax investigation in the requesting State were motivated by political, racial or religious persecution. The limitation may also be invoked when the information constitutes a State secret. For instance, there is no disclosure requirement when sensitive information is held by secret services, the disclosure of which would be contrary to the vital interests of the requested State. Thus, issues of public policy (*ordre public*) rarely arise in the context of information exchange between treaty partners.

22. As discussed above, paragraph 3 may give a requested State the right to refuse to supply information under some circumstances. It is not required, however, to invoke any of the limitations of that paragraph. If the requested State declines to exercise its right under paragraph 3 and supplies the requested information, the information exchanged remains within the framework of article 26. Consequently, the information is subject to the confidentiality rules of paragraph 2. In addition, the affected taxpayer or other third party has no ground for contending that the tax authorities in the requested State have failed to observe the obligation to secrecy imposed on them by domestic law.